

Supporting Statement for the Survey to Obtain Information on the Relevant Market in Individual Merger Cases (FR 2060; OMB No. 7100-0232)

Summary

The Board of Governors of the Federal Reserve System, under delegated authority from the Office of Management and Budget (OMB), proposes to extend for three years, without revision, the Survey to Obtain Information on the Relevant Market in Individual Merger Cases (FR 2060; OMB No. 7100-0232). The Federal Reserve designed this voluntary survey to determine from what sources small businesses and consumers in a particular geographical area obtain financial services. The Federal Reserve uses this information to define relevant banking markets for specific merger and acquisition applications and to evaluate changes in competition that would result from proposed transactions. The event-generated survey is conducted by telephone and has been used no more than four times per year since 1990 and only five times over the past three years. A copy of the survey form and instructions is provided as attachment 1. The current annual burden for the FR 2060 survey is estimated to be eighteen hours.

Background and Justification

Under the Bank Holding Company Act of 1956 [12 U.S.C. §§1841 *et seq.*], the Bank Merger Act of 1960 [12 U.S.C. §1828(c)], and the Change in Bank Control Act of 1978 [12 U.S.C. §1817(j)], the Federal Reserve Board is required to evaluate merger and acquisition applications by bank holding companies to determine the effects of proposed transactions on competition. The standards of the antitrust laws, specifically section 7 of the Clayton Act, must be applied. If a merger may substantially lessen competition or tend to create a monopoly, the Board shall not approve the merger.

The foundation for an analysis of competition by the Board in such merger applications is the economic concept of the relevant market. Applying the theoretical concept to specific situations requires the determination of the geographic area that includes all direct competitors (this area could be a town, a county, a state, a region of the country, or the entire country) and the relevant product market (this requires identifying the firms within the relevant geographic area that compete with one another).

For some time, there was widespread belief that the geographic markets in banking were local (for example, a single county) and that the product market was composed of commercial banking only. This definition was accepted and applied by the Supreme Court and accepted by the Board. However, as a result of substantial changes in banking and in the financial services industry as a whole in the past two decades, some have questioned the traditional definition of banking markets. The definition of a relevant banking market is essentially an empirical question. Prior to the implementation of the FR 2060 in 1987, there was no direct means by which to gather empirical evidence to assess the geographic scope of banking markets in specific situations. Although the findings of the Board's Survey of Small Business Finances (FR 3044; OMB No. 7100-0262) and the Survey of Consumer Finances (FR 3059; OMB No. 7100-0295) essentially confirm the validity of the local market approach as a general proposition, these findings will not necessarily apply in specific merger and acquisition cases. For consumer finances, the relevance of these findings can be ascertained only by conducting a survey such as

the FR 2060. Although the Federal Reserve now uses small business loan data from the Recordkeeping, Reporting and Disclosure Requirements in Connection with Regulation BB (Community Reinvestment Act) (OMB No. 7100-0197) as the primary source of information for analyzing small business financing, there are cases where the Federal Reserve uses the small business portion of the FR 2060 survey for supplemental information.

In its *Philadelphia National Bank* decision in 1963 and again in its *Connecticut National Bank* decision in 1974, the Supreme Court concluded and reaffirmed that banking should be treated as a distinct and separate line of commerce, and that only firms offering the full array of bank products should be included in the market definition of banking. Furthermore, the Court determined that banking markets for small businesses and consumers were limited to small geographic areas. Survey research conducted in conjunction with individual bank merger and acquisition cases between 1963 and 1974 supported this view.

Since the *Connecticut* decision, numerous changes in bank regulation, technology, and the economy have raised questions regarding the traditional definition of locally limited commercial banking. The most notable of these changes are:

- thrift institutions are now permitted to offer the majority of banking products, including transaction accounts and commercial loans,
- nondepository institutions offer various financial services,
- securitization and loan sales have increased, and
- electronic technology has increased the potential for very quick delivery of financial services to final users, including small businesses and consumers.

It is clear that large businesses have access to the national market, and in some cases the international market, for financial services. Moreover, for their large business customers, major U.S. banks compete with major foreign banks and the capital markets, particularly the commercial paper market. However, the empirical data compiled since the implementation of the FR 2060 survey in 1987 indicate that relevant banking markets for smaller businesses and customers are still generally limited to small geographic areas, such as a county or a metropolitan area and that there is a tendency to purchase a cluster of services from commercial banks. The data obtained from this survey have provided the Board with a more accurate picture of the relevant banking market for selected merger applications. This type of case-specific information on the market definition in merger applications has provided an empirical foundation for staff analysis, Board decisions, and published Board orders prepared by the Board's Legal Division.

The Federal Reserve conducts the FR 2060 survey only in those cases in which a potentially serious competitive issue arises, as determined through economic analysis at the Board and Reserve Banks. A case is flagged as such when the consideration of data on competition from readily available sources suggests that anticompetitive effects would arise from the proposed merger or acquisition. The survey data provide a valuable empirical foundation for the Board in considering the competitive implications of those proposed mergers that carry the greatest possibility of being challenged in court on their competitive issues.

Out of the several hundred bank merger and acquisition applications reviewed by the Federal Reserve each year, as required by law, fewer than three dozen are evaluated by the Board because they raise potentially serious competition problems. In a few of these cases, there is not sufficient data to allow a sound economic analysis as the basis for a decision by the Board and a written Board order by the Legal Division. In these cases, the FR 2060 survey provides useful information for analyzing competition or clarifying the market definition.

Description of Information Collection

The Federal Reserve conducts the survey by telephone. Information is obtained from approximately fifty consumers and approximately twenty-five small businesses selected at random from local telephone directories. The survey focuses on local consumers and businesses to determine whether, as in the past, they generally rely on local providers of financial services or instead obtain financial services from a broader geographic area such as a state or the entire country. In the survey of small businesses, responses are obtained from the most knowledgeable available individual, usually the president or treasurer. The sample selection process is described in attachment 2.

The survey questions serve as a guideline and were developed in consultation with staff from throughout the Federal Reserve who have considerable experience in defining relevant banking markets in cases where competitive issues arise. The questions were designed to assess the extent to which nonbank and nonlocal financial services are used by or offered to small businesses and consumers. The main objective of the questions is to determine the importance and influence of nonbank and out-of-area sources of credit and deposit services. In several merger and acquisition cases, the surveys have provided the Federal Reserve with key information for defining the relevant banking market and assessing competition. The Federal Reserve tailors the survey questions for certain mergers or acquisitions, as appropriate. An example of one of these tailored surveys is provided as attachment 3.

The survey data permit the use of statistical tests to determine the confidence that may be placed in the findings. Because the samples are drawn from a specific local market, the findings are valid for the particular case under consideration by the Federal Reserve, but extrapolation to other markets or to the nation as a whole is not appropriate.

Time Schedule for Information Collection and Publication

Generally within the first week after a Reserve Bank accepts a merger application, the Reserve Bank makes a preliminary evaluation of the possible effects on competition. If certain Board delegation criteria are not met, the Reserve Bank notifies the Board's Division of Research and Statistics, which analyzes the likely competitive effects and decides whether it would be advisable to conduct the survey. If a survey is deemed advisable, the appropriate Reserve Bank conducts the FR 2060 survey. The number of questions in the survey has been kept at a minimum so that the entire process of conducting the survey, tabulating the responses, and summarizing the findings can be finished within the confines of the Federal Reserve's internal sixty-day limit for processing merger and acquisition applications. Once the Reserve Bank has

summarized the responses of small businesses and consumers, the survey results are sent to the Division of Research and Statistics, where an economist analyzes the information and incorporates relevant findings into a memorandum to the Board of Governors. The responses are confidential and therefore are not published.

Legal Status

The Board's Legal Division has determined that this report is authorized by law [12 U.S.C. §1817(j), 1828(c), and 1841 *et seq.*] and is voluntary. Individual responses are confidential pursuant to the Freedom of Information Act [5 U.S.C. §§552 (b)(4) and (b)(6)] for small businesses and consumers, respectively.

Consultation Outside the Agency

There has been no consultation outside the Federal Reserve.

Estimate of Respondent Burden

The current burden for the FR 2060 survey is estimated to be eighteen hours annually as shown in the following table. Because the survey is event generated, it is not possible to predict exactly how many surveys will be conducted in a given year. The burden estimate shown in the table below is based on the average number of responses received during the past three years. This represents less than 1 percent of total Federal Reserve System annual reporting burden.

	<i>Number of respondents</i>	<i>Estimated annual frequency</i>	<i>Estimated average hours per response</i>	<i>Estimated annual burden hours</i>
Small Businesses	25	2	10 minutes	8
Consumers	50	2	6 minutes	<u>10</u>
<i>Total</i>				18

Based on an hourly cost of \$20, the annual cost to the public is estimated to be \$360.

Sensitive Questions

This collection of information contains no questions of a sensitive nature, as defined by OMB guidelines.

Estimate of Cost to the Federal Reserve System

The annual cost to the Federal Reserve of conducting the surveys is negligible.

Attachment 1

Attachment 2

Overview of the Sample Selection Process

Sampling Procedures

For the consumer component of the survey, the population of interest consists of all households located in the geographic area that the Reserve Bank defines as the market. The unit of observation is the household. The respondent will be the financial head of the household or a financially knowledgeable spouse.

For the business component of the survey, the population of interest consists of all business enterprises that had revenues of less than \$1,000,000 in the past year and that had an establishment in the designated geographic market area. However, there may be rare occasions where information from business enterprises with more than \$1,000,000 in annual revenue would be considered necessary. The unit of observation is the business enterprise. The respondent will be an individual who is responsible for the lending relationships and financial decision-making in the firm. That individual may be the owner, chief executive officer, president, treasurer, or comptroller.

A random sample will be drawn from listings in the local telephone directory using a random number table to select a page and then to select an entry on the page. The residential listings will be used for the consumer survey. The business white pages will be used for the business survey. In the event that business white pages do not exist, the yellow pages will be used.

The number of listings selected should be large enough to yield fifty completed household interviews and twenty-five completed business interviews. The proportion of blank listings (for example, listings with the number not working or that do not belong to a small business or household) and the response rate must be estimated to determine the number of listings to be selected.

A small number of screening questions will be required to determine whether a listing is an element of the population. If the survey yields substantially fewer than the desired number of completed interviews, perhaps because of an underestimate of the number of blank listings, then the first sample may be supplemented by a second random drawing. New listings, however, will not be allowed to substitute for refusals. Not at home will be treated as a refusal but efforts should be made to recontact.

Sampling Errors

The following tables present sampling errors, for the target sample sizes, across various hypothetical population sizes and across selected percentages of household or business respondents that do something asked in the survey

Table 1
Sampling Errors for Survey of Consumers
(Sample Size of 50 Households)

*Sampling error (plus or minus, in percentage points)
for a population of:*

Percentage of households that do something asked in the survey	2,000 households	4,000 households	10,000 households	20,000 households
90	9	9	9	9
70	13	13	13	13
50	14	14	14	14
30	13	13	13	13
10	9	9	9	9

Table 2
Sampling Errors for Survey of Business
(Sample Size of 25 Businesses)

*Sampling error (plus or minus, in percentage points)
for a population of:*

Percentage of businesses that do something asked in the survey	120 businesses	240 businesses	600 businesses	1,200 businesses
90	11	12	12	12
70	17	18	18	19
50	18	19	20	20
30	17	18	18	19
10	11	12	12	12

Attachment 3